

HUMBOLDT COUNTY ASSESSMENT PRACTICES SURVEY AND ASSESSOR'S RESPONSE

JULY 1998

CALIFORNIA STATE BOARD OF EQUALIZATION

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FOREWORD

The county assessor is responsible for the assessment of all taxable property within the county, except state-assessed property. The assessor's responsibilities include such things as (1) discovering and taking inventory of all property within the county, (2) determining a property's eligibility for a full or partial exemption from assessment, (3) determining the proper assessee who is usually but not always the owner, (4) determining the location for assessment purposes of the property, and (5) determining the taxable value of the property in accordance with California property tax law.

Determining taxable value is usually the most difficult and subjective of the assessor's duties. In addition to the inherently subjective nature of the appraisal process, the assessor also has to determine whether the taxable value is to be based on current fair market value or on a lower restricted value. When there is construction activity on a property, the assessor has to determine whether the construction is to be assessed or whether it is excluded from assessment under the law. When there is an ownership transaction, the assessor has to determine whether the law requires a reassessment of the property or whether the property must continue to be assessed according to the existing value base.

The factors discussed above, as well as others not mentioned here, contribute to making local property tax assessment a difficult tax program to administer. It is also a very important program since the property tax is one of the most important sources of revenue for local governments and public schools. For property owners it is a major annual tax burden, and, since it is normally paid in one or two large installments rather than many small increments, it tends to be more visible than most other taxes. Accordingly, proper administration of the property tax assessment program is vitally important both to the public agencies that rely on the tax and to the people who have to pay the tax.

Although the primary responsibility for local property tax assessment is a function of county government, the State Board of Equalization (BOE) has a number of duties in the property tax field imposed by the State Constitution and the Legislature. One of these duties, performed by the BOE's County Property Tax Division (CPTD), is to conduct periodic surveys of local assessment practices and report the findings and recommendations that result from the survey.

Assessment practices surveys are authorized by Government Code sections 15640 et seq. These code sections require each county's assessment practices to be the subject of such a survey at five year intervals. The surveys must include research in the assessor's office to determine the adequacy of the procedures and practices employed by the assessor in the assessment of taxable property, compliance with state law and regulations, and other required duties. The surveys may include a sampling of assessments from the local assessment roll to determine eligibility for the cost reimbursement authorized by Revenue and Taxation Code section 75.60.

The assessor was provided a draft of this report and given an opportunity to file a written response to the findings, recommendations and suggestions contained in the report. This report, the county assessor's response, and the CPTD's comments regarding the assessor's

response constitute the final survey report which is distributed to the Governor, the Attorney General, the State Legislature; and the county's Board of Supervisors, Grand Jury, and Assessment Appeals Board.

Fieldwork for this survey report of the Humboldt County Assessor's Office was conducted by the CPTD during March of 1997. This report does not reflect changes implemented by the assessor after the field work was completed.

The Honorable Raymond L. Jerland, the Humboldt County Assessor, and his staff gave us their complete cooperation during the assessment practices survey. We gratefully acknowledge their patience and good spirit during the interruption of their normal work routine.

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July 1998

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I. INTRODUCTION, SUMMARY, RECOMMENDATIONS AND SUGGESTIONS

A. INTRODUCTION

Regardless of the size of the county, the assessment of property for tax purposes is a formidable task. Proper administration of this task is vital both to government agencies in Humboldt County and to taxpayers. Because the job is so important and so complex, it is necessary for an independent agency such as the State Board of Equalization (BOE) to make periodic reviews of the assessor's operation. This survey report is the result of such a review of the Humboldt County Assessor's Office by the BOE's County Property Tax Division (CPTD).

Government Code section 15640, in part, mandates that the BOE shall:

" . . .(a) make surveys in each county and city and county to determine the adequacy of the procedures and practices employed by the county assessor in the valuation of property for the purposes of taxation and in the performance generally of the duties enjoined upon him or her... (c) The survey may include a sampling of assessments from the local assessment rolls sufficient in size and dispersion to insure an adequate representation therein of the several classes of property throughout the county....(f) The board shall develop procedures to carry out its duties under this section after consultation with the California Assessors' Association. The board shall also provide a right to each county assessor to appeal to the board appraisals made within his or her county where differences have not been resolved before completion of a field review and shall adopt procedures to implement the appeal process."

It is apparent from this language that the Legislature envisioned the BOE's office research and appraisal sampling to be parts of a single, connected process, i.e., the evaluation of how well the county assessor is carrying out his or her sworn duty to properly assess all taxable property on the local tax roll. This evaluation was to be based on office research, or in certain circumstances, office research and actual field appraisals of sampled roll items. The way in which the sampling and survey process is carried out was developed after consultation with the county assessors by the staff of the BOE's Property Taxes Department.

This survey was conducted according to the method mandated by Government Code section 15642. Following legislative direction, our survey primarily emphasizes issues that involve revenue generation or statutory mandate. This report is the culmination of a review of the Humboldt County Assessor's operation that consisted of the CPTD's office research that examined current practices and procedures in key areas to see if significant problems exist in the assessor's operation. Finally, the survey team offers positive courses of action, presented here as

recommendations and suggestions, to help the assessor resolve problems identified in his program.

Revenue and Taxation Code section 75.60 requires that the BOE certify a county as eligible for the recovery of costs associated with administering supplemental assessments. In order for a county to qualify as an eligible county, it must achieve an average assessment level that is not less than 95 percent of the amount required by law as determined by the BOE through its assessment sampling program. In addition, for sampling for the 1996 lien date and subsequent lien dates, the sum of the absolute values of the differences cannot exceed 7.5 percent of the legally required amount.

Based upon our sampling of the 1992-93 assessment roll, the BOE certified Humboldt County as an eligible county. This indicates that its assessment program is substantially in compliance with the law. The recommendations and suggestions contained in this report are based on our analysis of data which indicates that statutory violations, under-or-over assessments, or unacceptable appraisal practices may be occurring in specific areas.

B. SUMMARY

1. Survey Findings

Our comments on changes that would be beneficial for the Humboldt County Assessor's Office take the form of suggestions and recommendations. Suggestions are used where existing practices could be achieved more efficiently or economically. Recommendations are reserved for areas where violations of law may be occurring, tax revenue is being adversely affected by existing assessment practices, or improper appraisal procedures are being used.

Overall, we believe the assessor's program is sound and needs only "fine tuning." There are many areas of operation where we found that the assessor was conducting an excellent program. Some of these areas are described in the body of the report.

We have recommendations for changes to both the change in ownership and new construction assessment procedures, as well as in the areas of special property types and special procedures. This does not mean that the Humboldt County Assessor's programs suffer from any significant deficiencies; it simply suggests that there is room for improvement in several of the areas we checked.

We also make several recommendations for improvements in the business property program. The program's major deficiencies are an inaccurate method of developing replacement cost factors and depreciation tables and an unnecessarily time-consuming method of developing replacement cost estimates for individual items of business property.

2. Overview of Assessor's Office

The assessor is attempting to modernize his office's electronic data processing capabilities. In part, the goal of this effort is to fully integrate the assessor's, county auditor's, and county tax collector's information management systems that serve the property tax activity. This new system will make data more accessible, thereby providing statistical reports to be used for management's planning and control. In addition, public requests for information will be fulfilled in a more expeditious manner. This new system should provide more efficiency for work processes and make resources available for improving the quality of the assessor's overall operations. Hopefully, the additional resources will be available for implementation of the recommendations contained in this survey report.

The following information was taken from a document titled A Report on Budgets, Workloads, and Assessment Appeals Activities in California Assessor's Offices. The document is published annually by the State Board of Equalization. The assessor's staff has remained relatively constant between the 1991-92 and 1995-96 fiscal years. During this interval the property tax revenue generated for taxing agencies in the county has increased almost 27 percent

The gross budget of the assessor's office has declined 6 percent since fiscal year 1991-92; gross budget represents total expenses prior to any reimbursements for services furnished to others and/or financial aid from higher levels of government. Reimbursements and financial aid from others has decreased substantially since the 1991-92 fiscal year; the assessor's net budget has increased 175 percent since that year. The assessor's net budget for the 1991-92 fiscal year was \$537,482; for the 1995-96 fiscal year the net budget was \$941,849.

<u>Fiscal Year</u>	<u>Gross Budget</u>	<u>Staff Size</u> <u>(1)</u>	<u>Assessed Value</u>	<u>Number of</u> <u>Assessments</u>
1991-92	\$1,315,479	33	\$4,437,578,000	71,755
1992-93	\$1,253,327	33	\$4,739,936,000	72,136
1993-94	\$1,265,631	31	\$4,954,594,000	73,315
1994-95	\$1,420,746	31.7	\$5,294,357,000	73,881
1995-96	\$1,235,907	32	\$5,625,714,000	75,553

(1) includes assessor

C. RECOMMENDATIONS AND SUGGESTIONS

The following is a summary of the formal recommendations and suggestions contained in this report, arrayed in the order that they appear in the text. The page is noted where each recommendation or suggestion and its supporting text can be found.

Our recommendations are reserved for situations where one or more of the following conditions exist:

- Violations of state constitutional provisions, statutes, BOE regulations, or case law are present.
- Existing assessment practices result in the generation of an improper amount of property tax revenue.
- Existing appraisal practices do not conform to generally accepted appraisal practices.

RECOMMENDATIONS

- RECOMMENDATION 1: Revise the procedures for discovering and processing disaster relief assessments by: (1) regularly obtaining fire reports from all fire departments within the county; (2) maintaining better control of disaster relief claims; and (3) initiating a consistent procedure for granting relief when no application is returned. (Page 10)
- RECOMMENDATION 2: Add the cash equivalent value of improvement bonds to the nominal sale price of properties. (Page 15)
- RECOMMENDATION 3: Obtain copies of leases involving commercial properties. (Page 16)
- RECOMMENDATION 4: Revise the procedures for assessing new construction by: (1) including the value of water wells and septic systems in the assessments of single family residential properties; (2) applying appropriate depreciation to new additions; and (3) deducting the current assessed value of all improvements removed as a result of new construction. (Page 18)
- RECOMMENDATION 5: Revise CLCA assessments by: (1) deducting a charge for return on and of the investment in irrigation systems from the total property income; and (2) deducting a charge for capital replacement of irrigation wells that contribute to the income being capitalized. (Page 21)
- RECOMMENDATION 6: Revise the assessment of CLCA and TPZ parcels by using a nine year term to prepare the first assessment after a notice of nonrenewal has been filed. (Page 22)
- RECOMMENDATION 7: Assess land subject to the provisions of Article XIII section 11 of the California Constitution at the lowest of current market value, Article XIII A factored base year value, or section 11 value. (Page 23)

- RECOMMENDATION 8: Do not classify life estates as possessory interests. (Page 24)
- RECOMMENDATION 9: Assess private water company property at the lower of market value or factored base year value. (Page 25)
- RECOMMENDATION 10: Notify the county auditor of possible supplemental assessments caused by new construction. (Page 26)
- RECOMMENDATION 11: Revise business property valuation procedures by: (1) assessing property based on reported costs on annual business property statements; (2) using cost indices and percent good factors that are contemporaneous with the current lien date; and (3) discontinuing the practice of limiting the percent good in depreciation tables to an arbitrary minimum level. (Page 29)
- RECOMMENDATION 12: Assess computers by using the BOE's recommended factors. (Page 31)
- RECOMMENDATION 13: Comply with Property Tax Rule 461(d) when determining the proper appraisal unit for determination of taxable value; enroll the lower of the factored base year value or the current market value as the taxable value of each appraisal unit. (Page 32)
- RECOMMENDATION 14: Assign a certified appraiser the responsibility of determining boat values. (Page 37)
- RECOMMENDATION 15: Revise manufactured home assessments by: (1) classifying assessable manufactured homes on non-permanent foundations as personal property on the secured assessment roll; (2) enrolling the lower of the factored base year value or the current market value as the taxable value of all assessable manufactured homes; and (3) not applying the Article XIII A inflation factor to a prior year's market value estimate. (Page 39)

SUGGESTIONS

- SUGGESTION 1: Update the current ordinance to allow the assessor to grant a calamity reassessment when no application is returned. (Page 12)
- SUGGESTION 2: Increase documentation on assessment records. (Page 12)
- SUGGESTION 3: Improve CLCA appraisals by: (1) utilizing a questionnaire requesting production, income, and expense information on grazing lands; and (2)

recording the animal unit carrying capacity on each individual grazing land parcel. (Page 20)

SUGGESTION 4: Record the base year land values on Timberland Production Zone parcels that transfer. (Page 22)

SUGGESTION 5: Develop a more comprehensive audit program by: (1) maintaining a record of mandatory accounts with a four-year history of assessment amounts; (2) formalizing a nonmandatory audit program; and (3) using an audit checklist and a comprehensive audit narrative in every audit. (Page 33)

SUGGESTION 6: Improve audits by including the following topics in audits when appropriate: (1) flight and ground time for commercial airline companies; (2) income and expense data when it is used to value the property; and (3) interest during construction on large commercial and industrial properties. (Page 35)

II. ADMINISTRATIVE TOPICS

A. ASSESSMENT APPEALS

The assessment appeals function is established by Article XIII, section 16 of the California Constitution. Revenue and Taxation Code sections 1601 through 1645 are the statutory references that guide county assessment appeals boards. Government Code section 15606(c) directs the BOE to prescribe rules and regulations to govern local boards of equalization, and the BOE has adopted Property Tax Rules 301 through 326 of the California Code of Regulations, Public Revenue, to regulate assessment appeals.

A review of the appeals function involves both the activities of the county appeals agency and the activities of the assessor's office as they relate to assessment appeals. The two agencies must have a close working relationship in order to make the appeals process effective, particularly in the areas of case scheduling and document processing. At the same time, the statutory separation of the authority and responsibility of both agencies must be maintained.

Conformance to the Revenue and Taxation Code and property tax rules include adherence to the statutory filing periods (sections 1603, 1604, 1605); proper jurisdiction of the appeals board in regard to matters heard (sections 1610.8, 1613, and Property Tax Rule 302); eligibility requirements for board members and hearing officers (section 1624.05); and adequacy of written findings and conclusions (section 1611.5). The scope of this survey did not permit a thorough review of the above areas. However, a limited review of the Humboldt County assessment appeals program did reveal the following information.

The number of assessment appeals has dramatically increased during the recent seven year period of declining real estate values. Most of this increase in filings is based on section 51 of the Revenue and Taxation Code, which requires that real property, with few exceptions, be annually assessed at the lower of factored base year value or the current market value. An owner of property who believes that the current market value is less than the factored base year value is likely to request an assessment review. A review that does not satisfy the owner is likely to result in a formal assessment appeal.

The County of Humboldt is no exception to this trend. The table below summarizes the Humboldt County appeals workload. The period covered is the last four years, which shows a steady increase in the number of appeals. The totals for the last four years for Humboldt County are as follows:

<u>Assessment Year</u>	<u>Beginning Backlog</u>	<u>New Appeals</u>	<u>Total Workload</u>	<u>Appeals Completed</u>	<u>Ending Backlog</u>
1993-94	86	155	241	167	74
1994-95	74	206	280	103	177
1995-96	177	159	336	174	162
1996-97	162	191	353	134	219

On October 30, 1979, the Humboldt County Board of Supervisors adopted Humboldt County Ordinance No. 1364, which established the Assessment Appeals Board and the qualifications and duties of members.

Due to the time period for our survey, our examination of the county's assessment appeals functions was limited. We were unable to review an actual appeals hearing since no hearings were scheduled during the period of field work. However, we did review the assessor's appeals procedures and found them to be well structured.

With the exception of major appraisals, the policy of the assessor's office is for the individual appraiser to prepare and make the presentation before the appeals board for all appeals within that individual appraiser's area of responsibility. For the major appraisals, the chief appraiser handles the presentation and either handles or helps with the preparation.

After several post-session discussions with the members of the assessment appeals board, the assessor's staff was able to develop a detailed perception of what the board members were looking for in the assessor's presentations. As a result of these discussions, the assessor's staff was able to perfect an effective approach for responding to an appeal. This suggested approach is set forth, step by step, in the county's procedure manual.

We reviewed one recently appealed property which was presented before the assessment appeals board and found that the hearing materials prepared by the staff followed a standard format and were of high quality. The appraisal methods and techniques followed generally accepted standards. The value established by the assessor's staff was well documented and was upheld in the board's decision. In conclusion, we believe the county's overall assessment appeals program is well run.

B. ROLL CHANGES

The Revenue and Taxation Code provides several techniques by which an assessment placed on the local roll can be changed after the assessor has delivered the roll to the auditor. Roll changes are generally made under the following statutory provisions: section 4831 et seq. which provides for roll corrections due to errors or value judgments that did not reflect declines in value below factored base year values, and section 531 et seq. dealing with escaped assessments.

The changes to the assessment roll referred to here are made after the roll is delivered to the auditor. These changes cover all types of items such as late filed homeowners' exemptions, assessment appeals, corrections made by the assessor, or public land acquisitions.

The Humboldt County Assessor's Office has an excellent assessment procedures manual that describes the various types of roll changes and the procedures for their application to the roll. According to the chief appraiser and the supervising assessment technician for Humboldt County, all roll changes are initiated by the individual appraiser who has the responsibility for the area in which the particular property is located.

All roll changes are entered on the county form titled Assessor's Petition For Change Of Assessment. This form, together with all pertinent information, is submitted to the appraiser's supervisor for review. Upon approval, it is forwarded to the assessment recording section, which enters the information into their computer system. The assessment recording section will print and mail a Notice Of Proposed Escape Assessment and/or a copy of the proposed Assessor's Petition For Change Of Assessment to the assessee. This form letter contains a notice to the assessee that a change in assessment has been proposed, a brief explanation of the reason, and the time period for filing an appeal if the assessee wants to contest the change. A copy of the change order is sent to the Humboldt County Auditor's Office who will review it for the correct code citations, etc. If the roll change document is in correct form and the ten day waiting period has passed, the auditor will then process a tax bill and send it to the assessee.

We examined the records of a random sampling of various roll changes made during the 1996-97 roll year. We found that the assessor has done a very good job in recording roll changes utilizing the appropriate code sections. In those cases where there were discrepancies, we found the errors were of minor importance. Also, we found no pattern which would indicate a significant problem in the assessor's roll change program.

In conclusion, the overall review of the county's records indicates that the Humboldt County Assessor's Office is doing a very credible job in processing roll changes and should be commended for their efforts.

C. DISASTER RELIEF

Revenue and Taxation Code section 170 authorizes a county board of supervisors to adopt an ordinance that would provide property tax relief to an assessee whose property has been damaged or destroyed without the assessee's fault. The ordinance may be made applicable to a major misfortune or calamity within a region that has been declared a state of disaster by the Governor, or to any other misfortune or calamity, or to both. The misfortune or calamity need not be a widespread disaster such as flood or earthquake, but may be an isolated incident such as a fire or mud slide affecting only one or two properties. The ordinance may specify a period of time within which the ordinance shall be effective, or it may remain in effect until it is repealed.

Calamities or disasters can be due to acts of God (floods, avalanches, earthquakes, etc.), acts of man (war, crime, riots), accidents, and ordinary negligence. Not all calamities are "natural"; human agency is involved in many instances. The act of a tenant should not be imputed to the owner, absent a showing of collusion. The property owner should not be denied tax relief because of accidentally caused calamities.

To obtain relief under this ordinance, the following the conditions must be met: (1) the total loss in full cash value (not the taxable roll value) to land, improvements, and personalty must be at least \$5,000; (2) the calamity can not be due to the fault of the owner; (3) the application must be filed within the time specified in the ordinance, or, if no time is specified,

within sixty days of the misfortune or calamity; and (4) the application must show the condition and value, if any, of the property immediately after the damage or destruction, and the dollar amount of the damage.

However, when one's property is severely damaged or destroyed, it is conceivable that the taxpayer will not contact the assessor's office for an application for assessment. The taxpayers may not be aware of the rights granted by section 170 or may not think of filing an application because of other more demanding concerns. To mitigate this potential oversight on the part of a taxpayer, section 170(l) provides that if the assessor is aware of any property that has suffered damage by misfortune or calamity within the previous six months, the assessor may, with the approval of the board of supervisors, reassess the property and notify the last known owner of the reassessment.

Once a taxpayer has met the requirements for disaster relief, the assessor must calculate the percentage of the full cash value lost and that percentage must then be applied to the values appearing on the roll. The taxpayer is liable for a prorated portion of the taxes that would have been due on the property for the current fiscal year had the misfortune or calamity not occurred, plus a proration of the tax due on the property as reassessed in its damaged condition. Any taxes paid in excess of the total tax due must be refunded to the taxpayer, without the necessity of a claim being filed by the taxpayer, as erroneously collected tax.

The Humboldt County Board of Supervisors, upon the request of the assessor, adopted ordinance No. 1473, which provided for the reassessment of property damaged by misfortune or calamity. This ordinance was adopted on the 2nd day of June 1981 and is published in section 751-2 of Title VII of the Humboldt County Code.

According to the assessor's procedures manual, when an appraiser becomes aware of a misfortune or calamity, the appraiser should notify the assessment technician responsible for sending out and recording the receipt of the proper claim form. The property record should then be flagged for a recheck. When the property is repaired, the taxable value is to be restored to its properly factored base year value. The value reductions for property damaged or destroyed may be done through the supplemental assessment roll, as are restorations of value upon completion of repair.

RECOMMENDATION 1: Revise the procedures for discovering and processing disaster relief assessments by: (1) regularly obtaining fire reports from all fire departments within the county; (2) maintaining better control of disaster relief claims; and (3) initiating a consistent procedure for granting relief when no application is returned.

Fire Reports

In our survey fieldwork we found that for the 1996-97 roll year, 14 applications for calamity reassessment were sent to the owners of record for properties which appeared to have met the requirements as provided under the provisions of Revenue and Taxation Code

section 170. According to the assessment technician responsible for sending and recording the receipt of the claim form, the assessor's staff relies primarily on newspaper articles, taxpayer notifications, field investigations, building permits and, to a limited extent, information from some fire districts for discovering calamities or misfortunes.

In the Humboldt County Assessment Practices Survey for 1990, we found that the assessor's staff was not receiving consistent reporting from the various fire districts within the county. In that report, we suggested that the assessor obtain regular fire reports from all fire districts in the county.

We examined the records of all 14 properties that had known potential applications for calamity reassessments during the 1996/97 roll year and found that there is currently no reporting from the county or any of the various city fire departments nor from the State Department of Forestry. The only information on fires that occurred within some of these districts was obtained by members of the assessor's office who were volunteer members of the respective fire districts.

Of the 14 known potential applications for the 1996/97 roll year, only seven were completed and returned to the assessor; of these seven, adjustments were made on six properties, while one property consisted of construction without a permit that had escaped assessment for which no adjustment was necessary. Of the seven applications that were not returned to the assessor, adjustments were made on four assessments; two property records indicated no adjustments were made due to various circumstances; and one property record had no reference to any fire report.

In addition to these 14 properties, we examined records of various properties that had fire damage for which no adjustments have been processed by the assessor's staff. We obtained information on these instances of fire damage by contacting three fire districts which issue the majority of all fire reports in the county. The three fire districts were the City of Eureka, the Humboldt Fire Protection district, and the State of California's Department of Forestry located in Fortuna.

We examined the appraisal records of 29 properties for which these three fire protection agencies had reports indicating fire damage in excess of \$5,000. We found that only six had disaster relief adjustments; two of the six with adjustments had no application in the file.

Our review indicates that the assessor's procedures on disaster relief are not being followed. We found that the assessor has not been receiving fire reports from any fire districts. Therefore, we once again recommend that the assessor regularly obtain fire reports from all fire districts within the county.

Control System and Consistency of Procedures

Our current review disclosed the absence of a good control system for calamity reassessment applications. In some instances we found that the assessment technician, who is

responsible for keeping track of calamity damaged properties, was not aware when an application was returned and therefore no acknowledgment was recorded. Additionally we found the following problems: (1) no adjustments or follow-ups to fire reports with losses estimated at \$19,000 to \$50,000 or more; and (2) where the applications were not returned, the county appears to be inconsistent when granting adjustments. In some cases adjustments were made while in many others no adjustments were acknowledged and few if any comments were made.

We recommend that the assessor initiate a more stringent supervisory system whereby all disaster claims meet the required steps as prescribed in the assessor's procedures manual.

County Disaster Relief Ordinance

Revenue and Taxation Code section 170(l) allows a county to adopt a disaster relief ordinance that provides for disaster relief without a taxpayer filing a written application. If such an ordinance is in effect, the assessor may, with the approval of the board of supervisors, reassess the property as described in section 170 and notify the last known owner of the property of the reassessment.

SUGGESTION 1: Update the current ordinance to allow the assessor to grant a calamity reassessment when no application is returned.

Humboldt County's Ordinance No. 1473, which addresses disaster relief assessment changes, states that upon *receiving* a proper *application* the assessor, the auditor, and the board of equalization shall follow the procedures prescribed by Revenue and Taxation Code section 170 when processing the application. This would seem to require that the application for disaster relief be filed by the taxpayer. We suggest that the county update the current ordinance granting the assessor authority to grant relief when no application is made.

D. DOCUMENTATION

The assessor is to be commended for the Assessor's Procedures Manual his staff recently produced. One weakness we did observe in the real property section of the manual is that it did not emphasize the need for documentation on the assessment records. To determine the significance of this perceived weakness, we reviewed many of the assessment records from our sampling of the 1992-93 Humboldt County assessment roll in addition to numerous other files. This topic was the subject of a suggestion in our 1990 Humboldt County Assessment Practices Survey.

SUGGESTION 2: Increase documentation on assessment records.

The assessor's current policy does not require documentation on the assessment record of building permits that do not require revision of the base year value or the source of replacement cost new estimates unless a source other than the BOE is used. While individual permits may not generate a need for revision of the base year value, an accumulation of permits

on a property in a short period of time could indicate the need for such a revision. Without knowledge of the prior permits, the assessor's staff cannot reach a sound conclusion regarding the issue. If the source of replacement cost new estimates is not indicated on the assessment record, a subsequent reviewer is placed in the position of having to assume that BOE costs were used when in fact the lack of documentation of an alternative source of the cost may be an oversight.

Assessment records should clearly document the reason for acceptance of sale price as the base year value. The documentation relating to change in ownership could be a simple boilerplate statement to the effect that the fee simple absolute rights to the property were transferred and that the conditions of the sale met the requirements of Revenue and Taxation Code section 110(a).

We found that the some of the possessory interest files lacked current leases, permits, or other written instruments that established the possessory interest. Documenting the file is a necessary first step in valuing the possessory interest; without such documentation, it can be difficult to ascertain the term of possession, economic rent, date of change in ownership, ownership of improvements upon reversion, and other facts essential to a sound appraisal. We suggest that the assessor increase the documentation of these files by obtaining a copy of each tenancy agreement.

We suggest the assessor direct his staff to increase documentation on the assessment records in order to support the base year values created as a result of change in ownership; by recording all building permits and the source of replacement cost factors; and by including the tenancy agreements for possessory interests.

III. REAL PROPERTY VALUATION AND ASSESSMENT

A. THE APPRAISAL PROGRAM

1. Overview

The BOE last conducted an appraisal sample for Humboldt County for the 1992 lien date. The sampling results do not indicate any system problems or any particular weakness in the assessment programs.

Our sample of the 1992-93 assessment roll contained 56 sample items that were classified as change in ownership. Of these, only one showed a difference between the BOE staff's and the assessor's estimates of taxable values. This instance involved a subjective judgment regarding the value of the sample property.

Also during the sample our staff found 27 instances of value differences related to new construction. Value differences resulted from 12 instances involved escaped assessments due to new construction performed without a permit; and 15 instances involved subjective judgments, including differences of opinion about the estimate of replacement cost new and differences regarding the appropriate amount of depreciation accruing to newly constructed additions to real property.

The assessor's staff concurred with the CPTD's value for four of the 16 instances of underassessment. Three of the four instances involved escape assessments and the fourth pertained to the proper estimate of percent good for an addition to an existing structure. The three escape assessments consisted of a hot tub, new wells, and septic tanks. In seven instances involving escape assessments, the assessor's staff revised the roll values to reflect the appropriate valuation.

2. Change in Ownership

a. Transfers

There were 3,297 parcels that changed ownership in Humboldt County during the 1995-96 fiscal year that required reappraisal. This was a decrease from a 3,650 parcel annual average for the previous three years.

Revenue and Taxation Code section 110(b) and the California Administrative Code, Title 18, Public Revenue, Rule 4 require the assessor to accept the cash equivalent selling price as the market value of the sold property unless "a preponderance of the evidence" indicates otherwise. Rule 4 places the burden of proof for rebutting this presumption on the person attempting to overcome the presumption. The preponderance of evidence refers to the conditions of sale referred to in Revenue and Taxation Code section 110(a) as well as the difference between sale price and appraised value being a minimum of 5 percent of the sale price. The Humboldt County Assessor has compliance with this statutory requirement as an essential

element of his real property assessment program, and the office procedure manual instructs the staff to implement this concept.

Essential to correct implementation of this presumption is an understanding that the property rights that are subject to property taxation are the unencumbered fee simple absolute rights. If those are the property rights transferred, a comparison of the sale price to an appraised value is not routinely required. An example of when a transfer would not include those rights would be the purchase of a property by a lessee; the lessee already has an interest in the property (the leasehold interest) and the sale price would ordinarily reflect the net amount after deduction of the value of the leasehold interest. In that instance a comparison of the sale price to an appraised value would be appropriate.

The vast majority of the assessment records we reviewed indicated the assessor's staff accepted sale price as the new base year value. In such instances the records did not indicate that the assessor's staff had attempted to calculate an estimate of market value to compare with sale price. There is no requirement that such a comparison be routinely made. However, a statement on the assessment record to the effect that such a comparison was not necessary would be appropriate.

During our review we did not find any problems with the base year values relating to change in ownership caused by transfers of property with the exception of the assessor's treatment of cash equivalency adjustments. This issue is discussed in the following text.

b. Improvement Bonds

Improvement bonds are a form of public financing used to finance construction of municipal improvements. They are a lien on specific land parcels in specific amounts. Examples of such improvements are sewers, sidewalks, lighting, and water lines. Bonds issued under the Improvement Bond Act of 1911, Municipal Improvement Act of 1913, and the Improvement Bond Act of 1915 are first liens against property. A bond can be subordinated only to a previously issued bond. Pursuant to Property Tax Rule 4(b), the appraiser should add the present value of the bond payments to the nominal sale price of the property when using the comparative sales approach to value. This cash equivalency adjustment is equally applicable when the sale price of a property is accepted as the market value of the property.

To assist the assessor's staff in acquiring information on improvement bonds, Revenue and Taxation Code section 163, effective January 1, 1996, requires any entity that receives revenue from an assessment lien created by one of these bonds to annually notify the assessor of (1) the lien amount on each subject parcel at the time the lien was created; (2) if the lien has been completely satisfied, the date and amount of payment in satisfaction of the lien and identity of the party that made the payment; (3) the amount of the principal balance of the lien on each subject parcel.

RECOMMENDATION 2: Add the cash equivalent value of improvement bonds to the nominal sale price of properties.

Records obtained from the auditor-controller's and tax collector's offices show that there are seven 1911, 1913, and 1915 Bond Act issues with outstanding principal balances in Humboldt County. We reviewed a subdivision in the McKinleyville area with 1,597 parcels encumbered with bonded indebtedness. The original 1977-78 assessments on the parcels we reviewed were \$1,170 to \$2,295 per parcel; the present balance of the bond debt varied from \$427 to \$790.

The chief appraiser informed us that their office does not add the present value of improvement bonded indebtedness to the nominal selling price of real property. Even though balances on bond debts may be small, the appraisers should be aware of them and make the proper cash equivalent adjustment. We recommend that the assessor's staff identify sold properties encumbered with improvement bonds and adjust the nominal selling prices by adding the present value of the payment amounts remaining at the time of sale. The nominal sale price adjusted by the bonded indebtedness is a value indicator; it does not necessarily represent market value. The reliability of the indicator must be resolved by the appraiser prior to being enrolled as market value.

c. Legal Entity Ownership Program (LEOP)

The BOE's Policy, Planning, and Standards Division (PPSD) LEOP unit transmits to each assessor a listing, with corresponding property schedules, of legal entities that have reported to PPCSD that a change in control of the entity has occurred. Each of the reported changes in control transactions are investigated by PPCSD. The report includes the names of acquiring entities, the date stocks or partnership interests transferred, the parcels involved, and whether the property was owned or leased on the transfer dates.

Not all of the acquiring entities are able to provide detailed information such as the name of the county where the property is located, the assessor's parcel identification number, or how many parcels are owned by the entity. Because of the potential for inaccuracies in the data provided by the entities, PPCSD has advised the assessors to thoroughly research the named entity's holdings to ensure that all affected parcels are identified and properly appraised.

Revenue and Taxation Code section 61(c) states that a change in ownership of real property occurs with the creation of a leasehold interest in taxable real property for a term of 35 years or more (including renewal options). Therefore, when such a lease is created, the property involved should be revalued. Conversely, if a property is sold while encumbered with a lease having a remaining term of 35 years or more (including renewal options), Revenue and Taxation Code section 62(g) excludes the sale transaction from the definition of a change in ownership.

RECOMMENDATION 3: Obtain copies of leases involving commercial properties.

This was a recommendation in our previous report on Humboldt County. Our current review disclosed that the assessor had not obtained lease information on commercial

properties that were on PPSD-LEOP's listing of legal entities reported to have a change in control. Commercial malls and shopping centers may have long term leases in effect, and lease information should be obtained to help determine whether or not the property, in whole or in part, is subject to revision of the base year value.

In two instances we observed, PPSD notified the assessor of a change in control of a legal entity with a lease for portion of two properties in Humboldt County. For one of the properties, the assessment record did not indicate a revision of the base year value. The only pertinent remark on the assessment record was that change in control had occurred; the appraiser who reviewed the assessment did not have any information on the lease. For the other property, the base year value for the entire shopping center was changed without obtaining lease information.

The chief appraiser informed us that the office has recently started to collect rental data on commercial properties. However, there is no formal written policy for obtaining lease information in the Assessor's Procedures Manual.

A sound appraisal requires developing all appropriate value indicators. Without extensive lease information, it is not possible to arrive at capitalized income value indicators for such properties. A valid decision regarding a change in ownership and the need for a new base year value is not possible without analyzing lease information.

We recommend the assessor obtain copies of leases involving income-producing properties with emphasis on large and complex properties

3. New Construction

In Humboldt County there are eight local permit-issuing agencies. These agencies represent the County of Humboldt and the Cities of Arcata, Blue Lake, Eureka, Ferndale, Fortuna, Rio Dell, and Trinidad. In the fiscal year 1996-97, these agencies, with the exception of the Cities of Blue Lake and Trinidad, issued 3,146 permits, of which 1,152 were considered by the assessor's appraisal staff to be assessable new construction. Between 1990-1997, these same agencies issued an average of 3,899 permits annually of which an average of 1,736 annually were assessable new construction.

a. Assessment of New Construction

In many instances, the only practical approach to valuing newly constructed property, particularly additions, is the cost approach. The historical cost has become a heavily utilized technique for the valuation of assessable new construction. When the known costs are full economic costs they may be used to value newly constructed property, unless the appraiser has sales data that indicate these costs do not correspond to market value. In the absence of historical costs and lack of adequate sales data, costs obtained from reliable published cost guidebooks will suffice as good indicators of value.

When estimating value by the use of the cost approach, it is proper appraisal practice to make adjustments to the replacement cost new for depreciation that has accrued to the entire improvement. A percent good factor, which is appropriate for the entire improvement, should be applied to replacement cost new of the newly constructed addition. This is especially true when an addition is made to much older structures.

RECOMMENDATION 4: Revise the procedures for assessing new construction by: (1) including the value of water wells and septic systems in the assessment of single family residential properties; (2) applying appropriate depreciation to new additions; and (3) deducting the current assessed value of all improvements removed as a result of new construction.

The assessor's policy for estimating replacement cost new for single family residences does not require the addition of the cost of installing wells and septic tanks or recording those items on the assessment records. The assessor's staff indicated that it was their understanding that such property items are included in the residential building unit cost factors published by the BOE.

Their understanding is not completely accurate. The residential unit cost factors published by the BOE include the cost of physically connecting the water and sewer hookups in an urban environment. If paid at the time of the issuance of the building permit, the cost factors also include the sewer and water connection fees (the buy-in to the systems). However, the timing for payment of these fees may vary by locale; this variation is one of the reasons for location adjustments. The BOE method of deriving these costs is based on the sale price of a total property less the site value. If the site values include the cost of sewer and water permit fees, then the residual that is attributed to the structure does not and therefore the cost factors do not include such costs. However, the costs of wells and septic tanks are not included in these cost factors. Assessors' Handbook 531.10 on pages 1 and 2 describes the type of cost included in the square foot cost factors. The costs of wells and septic tanks must be added separately to the replacement cost estimates of properties that are not connected to municipal systems. We recommend the assessor add the value of wells and septic systems when improvements are connected to these items.

It is proper appraisal practice to make adjustments to the replacement cost new for depreciation that has accrued to the entire improvement. A percent good factor, which is appropriate for the entire improvement, should be applied to replacement cost new of the newly constructed addition. This is especially true when an addition is made to much older structures.

In reviewing CPTD's sampling of the Humboldt County 1992-93 assessment roll and current assessor's records for new construction, we found a number of instances where the county assessor's staff improperly treated additions to existing structures as separate appraisal units and assessed the additions at the full cost of construction. However, it is proper appraisal practice to consider the total improvement as the appraisal unit and use the percent good of the existing structure or a "blended" percent good, whichever is representative of the remaining

economic life of the entire structure. Of course, if the original structure had a very high percent good, the appraiser may wish to add the full replacement cost of the addition.

We recommend that the assessor's staff adjust the total costs of an addition by applying a percent good factor appropriate for the total structure including the new addition. We refer the assessor's staff to the assessment practices survey entitled A Report on The Assessment New Constructed Property and Property Under Construction (1982).

Revenue and Taxation Code section 75.10(b) states that the definition of new construction includes the removal of a structure from land. The section requires that the new base year value of the remaining property (after the removal of the structure) be determined in the same manner as provided in of section 51(c).

We found four instances where the value of a demolished improvement was not removed from the current assessment roll. The appraisal records did not address the value of the structures that the permit indicated were to be removed. The only value change that occurred was that the value of the new structure was added to the current assessed value. There was no indication as to whether the value of the demolished structure was deducted from the factored base year value. In addition to these cases involving replacement construction, we reviewed a property where the permit involved the demolition of all existing improvements without any new construction. In this instance, the property had a well and septic tank included in the improvements. The county removed the total assessed value without assigning a separate value to these items. Where the improvements included wells and septic tanks, a value should be assigned to these items and maintained in the current roll value for improvements.

We recommend that the assessor's staff remove the value of demolished improvements from the assessment.

B. SPECIAL PROPERTY TYPES

1. Restricted Value Property

a. California Land Conservation Act (CLCA) Properties

An agricultural preserve is established between a landowner and the county pursuant to the California Land Conservation Act of 1965 (CLCA). Land under contract must be assessed on the basis of its agricultural income-producing ability, plus any compatible use income (e.g., hunting, communications facilities, sand and gravel operations, etc.). These lands are assessed at the lowest of the restricted value required by the existence of the CLCA contract, the current market value, or the factored base year value, pursuant to Article XIII A of the California Constitution. Revenue and Taxation Code sections 422 through 430.5 deal explicitly with assessment of lands subject to agricultural preserve contracts.

For the 1996 lien date Humboldt County had 196,256 acres consisting of 1,542 parcels encumbered by CLCA contracts. Two of these contracts totaling 1,723 acres were in non

renewal status. None of the calculated restricted values were higher than the factored base year values. The total taxable value of the land was \$18.7 million; this is less than four-tenths of one percent of the net secured roll. According to the Annual Crop and Livestock Report published by the county Agricultural Commissioner, less than 1 percent of agricultural land in Humboldt County (not including timber) is cultivated. Grazing consists of about 334,000 acres; slightly over 19,000 acres of grazing land is irrigated pasture.

Procedures

One senior property appraiser is responsible for the values on all CLCA properties in Humboldt county. Presently, all CLCA property values are manually calculated each year. The assessor plans to have a computerized CLCA property appraisal program operating for the 1998 lien date. In addition to the CLCA workload, the senior appraiser also appraises all rural property not restricted by CLCA contract; and he is also assigned a geographic area within which he is responsible for the appraisals resulting from new construction and change of ownership events.

Procedures for assessment of CLCA properties were recently added to the Humboldt County Assessor's Procedures Manual. The procedures are clear and concise. However, further elaboration is needed on uniform guidelines for assessing these types of properties.

Sources Of Data

The assessor's staff does not use annual rent and production questionnaires to develop economic rents for animal unit months (AUM's). In the past an appraiser, who recently retired, met periodically with a "range land study group" to obtain income and production data. This group included county ranchers and the University of California Agricultural Extension area specialists.

SUGGESTION 3: Improve CLCA appraisals by: (1) utilizing a questionnaire requesting production, income, and expense information on grazing lands; and (2) recording the animal unit carrying capacity on each individual grazing land parcel.

As was discussed in our prior survey of the Humboldt Assessor's office, we suggest that the senior appraiser develop a questionnaire requesting information on carrying capacity, expenses, and income from grazing and compatible uses. This questionnaire should ask for the type of grazing operation (i.e., cow/calf, stocker, or both), number of head, months grazed, average weight and gain, supplemental feed required, and rent and expenses. The questionnaire should be mailed to each owner of grazing land in the county, regardless of whether or not their lands are under CLCA contract, thus obtaining a broader range on rental data.

The assessor's staff base their grazing land rents on the estimated number of AUM's a ranching operation will carry and then allocate the average rent of the total operating

unit to each land parcel in the unit. Assessors' Handbook section 521, The Appraisal of Agricultural Property, suggests that the total value of each grazing unit should be allocated to individual land parcels in the unit according to the carrying capacity of each parcel. It is improper to place an average value per acre on the total unit. Similarly, areas of significantly different capacity within a parcel should be separately estimated. We suggest that the appraiser, when valuing CLCA grazing lands, make proper allocations to each parcel based on productivity and that supporting data be documented.

RECOMMENDATION 5: Revise CLCA assessments by: (1) deducting a charge for return on and of the investment in irrigation systems from the total property income; and (2) deducting a charge for capital replacement of irrigation wells that contribute to the income being capitalized.

Income from irrigated land that is serviced by a permanently-installed irrigation system includes income attributable to the irrigation system. Nonliving improvements that are not subject to the CLCA contract, such as irrigation systems, are assessed separately from the property that is subject to the CLCA contract. Because these separately assessed unrestricted irrigation systems contribute to the land income that is capitalized into a CLCA land value, an amount for return on and of the investment in these irrigation systems must be deducted from the income stream. If this adjustment is not made the CLCA land value will include some value for the separately assessed assets, thereby creating a double assessment.

Another expense we found not accounted for by the county was an expense allowance for capital replacement for wells that contribute to the earning ability of the land being appraised. Wells may be the sole source of water supply, or used for supplemental water in an irrigation district. They are classified as land for property tax purposes and a return on investment is included in the land income. Nonetheless, they are a wasting asset and a charge for replacement must be subtracted from the land income.

We suggest using the replacement cost new (RCN) of the well when deriving a charge for replacement, i.e., if the replacement cost of a well on 300 acres is \$60,000 and the estimated life is 25 years, the charge would be \$8.00 per acre ($\$60,000 \times 4.0\% / 300 \text{ acres}$). Appraisers should be aware that lives on irrigation wells vary greatly. There are areas where wells will produce efficiently for 50 or more years, while in other locations wells will require replacement in 10 to 12 years.

We recommend the assessor include in his CLCA appraisal program a procedure that will calculate the proper charges for return on and of non-living improvements, and replacement of irrigation wells.

b. Timberland Production Zone (TPZ) Property

Land that has been classified as Timberland Production Zone (TPZ) is subject to assessment in accordance with the special TPZ site classifications that exclude the value of the standing timber. There are 7,046 parcels of TPZ land totaling about 985,000 acres in Humboldt County. The total 1995 timber harvest was 491.8 million board feet, valued at \$235.53 million.

CPTD's 1992-93 roll sampling of Humboldt County contained 23 sample items identified as TPZ parcels. CPTD staff found that the assessor had properly identified timber site classes for all 23 samples. Structures and building sites are also properly assessed. The valuation of 22 sample items were in agreement. The disagreement on one sample was the result of new construction escaping assessment because no building permit was issued; the assessor has since enrolled the escape.

For the 1997-98 assessment roll the assessor is using a computer program that computes the values on all TPZ properties, including TPZ lands with contracts terminating under section 426 of the Revenue and Taxation Code. However, the value of nonexclusive compatible uses is not included in the computerized calculations but is included in the assessment when such uses are present.

SUGGESTION 4: Record the base year land values on Timberland Production Zone parcels that transfer.

When properties zoned for TPZ change ownership, the assessor does not indicate on the appraisal records the unrestricted base year values. We suggest the assessor indicate the market values, as if unrestricted at time of transfer, on the appraisal records. This will assist in enrolling a proper base year value when a property is withdrawn from a TPZ zone under Revenue and Taxation Code section 426.

c. Terminating Contracts

The statutes relating to the assessment of properties encumbered with CLCA contracts or zoned as TPZ have provisions requiring the assessor to phase out the benefits arising from the contracts/zoning once a notice of nonrenewal of the contract/zoning is received. These provisions are contained in Revenue and Taxation Code section 426 and Government Code section 51120. The essence of the process is that the current taxable value is to be the restricted capitalized income value plus the market value or the factored base year value of the property at the termination of the contract discounted for the remaining term of the contract.

RECOMMENDATION 6: Revise the assessment of CLCA and TPZ parcels by using a nine year term to prepare the first assessment after a notice of nonrenewal has been filed.

The appraiser is properly calculating the two parcels with CLCA contracts currently in nonrenewal status and the 51 parcels with TPZ zoning being terminated except for

using a ten year discount period on the first calculation after the notice of nonrenewal is filed. The discount period is the number of years remaining until the termination of the enforceable restriction; therefore, the first computation after a notice of nonrenewal will be for a term of nine years (see Government Code section 51244.5). We recommend the assessor make the appropriate corrections on the parcels encumbered by these two CLCA contracts.

2. Taxable Government Owned Property

The Constitution of the State of California exempts from taxation property owned by a local government except lands and the improvements thereon that are located outside its boundaries and that were subject to taxation at the time of acquisition (Article XIII, sections 3 and 11(a)). Taxable government owned properties are frequently referred to as section 11 properties and must be assessed in accordance with the procedures specified in Article XIII, section 11, of the California Constitution.

The California Supreme Court decided in *City and County of San Francisco v. County of San Mateo, et al.* (1995, 10 Cal. 4th 554) that under Article XIII A of the California Constitution that the full cash value of section 11 lands was the assessment roll value for the 1975-76 tax year. The court determined that Article XIII A did not exclude from its valuation limitations taxable lands owned by local governments and located outside their boundaries. The court concluded that both Article XIII A and Article XIII, section 11, could be applied to such lands without conflict. The 1975 roll value, which was the lower of the fair market value or the 1967 assessed value times the “Phillips Factor,” became the base year value for these properties. The taxable value of the land must be the lowest of (1) the 1967 assessed value adjusted by a factor supplied annually by the State BOE of Equalization (section 11 value), (2) the current fair market value, or (3) the factored base year value.

Additionally the maximum taxable value of any improvement is established when acquired by the local government. The assessor subsequently enrolls the lowest of the factored base year value, the current market value, or the highest value ever used for taxation. Improvements constructed subsequent to the acquisition are exempt unless a structure replaces one that existed prior to acquisition by the agency. In that case, the value of the replacement cannot exceed the highest value placed on the original structure.

RECOMMENDATION 7: Assess land subject to the provisions of Article XIII section 11 of the California Constitution at the lowest of current market value, Article XIII A factored base year value, or section 11 value.

The Humboldt County Assessor has enrolled 30 section 11 properties. None of these properties has been properly assessed. None of the 30 section 11 parcels has been reviewed for the Article XIII A value limitation. For 23 of these properties the section 11 land values were calculated using the 1966 taxable value adjusted by the 1966 “Phillips” factor; they should have their section 11 land values calculated using the 1967 taxable value and the 1967 “Phillips” factor supplied by the BOE. The assessed value of the land should be the lowest of: (1) the 1967 taxable value adjusted by a 1967 “Phillips” factor; (2) the current fair market value; or (3) the

Article XIII A factored base year value. The records indicate that the lowest land value is the XIII A factored base year value.

We recommend that the assessor prepare these assessments in conformity with the California Supreme Court's decision in *City and County of San Francisco v. County of San Mateo et al.* (1995, 10 Cal, 4th 554).

3. Possessory Interests

The term "possessory interest" means an interest in real property which exists as a result of possession, exclusive use, or a right to possession or exclusive use of land and/or improvements unaccompanied by the ownership of a fee simple or life estate in the property. "Taxable possessory interest" means a possessory interest in nontaxable and taxable publicly owned real property as described in the California Constitution, sections 3(a), (b) and 11. Taxable possessory interests (PI) are further described in the California Code of Regulations, Title 18, Division 1, Chapter 1, Rule 21.

In Humboldt county one appraiser is responsible for appraising over 1,000 PI's in real property owned by approximately 100 public agencies. The appraiser has done a very thorough job appraising and discovering new PI's. Each year the appraiser examines records at the fairgrounds office to determine if there are any new PI's. Boat slips are reviewed on a yearly basis at the Humboldt Harbor District at Woodley Island and at the Eureka Boat Basin. The assessor's office also receives a listing of boats slips from the business office at city hall.

RECOMMENDATION 8: Do not classify life estates as possessory interests.

We discovered parcels located on Bureau of Land Management (BLM) property where the occupants had a life estate interest in the land. The occupants had retained the life estates when the land was sold to the BLM. The parcels are assessed as a possessory interest and at a base year value PI value lower than the fee value.

Retained life estates are not subject to assessment as PI's but are to be assessed in the same manner as fee owned parcels. Revenue and Taxation Code section 60 defines a change in ownership as transfer of a present interest in real property, including the beneficial use thereof, the value of which is substantially equal to the value of the fee interest. Section 62(e) specifically excludes a retained life estate from the definition of change in ownership. Property Tax Rule 21 specifically excludes a life estate from the definition of a taxable PI.

We recommend that the assessor not assess life estates in government owned property as taxable PI's but instead assess such life estates in the same manner as privately owned fee simple property is assessed.

4. Water Company Property

For property taxation purposes, water companies are generally classified as either private, mutual associations, or privately owned public utilities. In addition, publicly owned water systems outside the boundaries of the owner are also taxable to the extent that they consist of real property that was taxable at the date of acquisition (Article XIII, section 11 of the California Constitution). Generally, any nongovernmental entity that earns a profit from the sale of water is subject to regulation by the California Public Utilities Commission (CPUC). Proper characterization as to the type of entity is imperative because each type of water company requires different valuation techniques for the proper estimate of market value of its taxable property.

In Humboldt County, there are both private water companies regulated by the CPUC and mutual water companies. The previous survey of the Humboldt County Assessors Office contained a recommendation and suggestion regarding the assessment of property owned by both types of companies.

Private Water Companies

Private water companies are privately owned entities in business to earn a profit from the sale of water. When these companies are subject to regulation by the CPUC, they must submit annual financial reports on their operations to the CPUC. The CPUC regulates the rates charged by these companies; profits are limited to a fair return on the companies' outstanding investment in their net assets, i.e., the historical cost less depreciation (HCLD).

Because profit is tied to a declining book investment, the market value of the water company may also have declined. As a result, the current market value of the company may be less than its factored base year value, making it necessary to annually determine the company's taxable value as of lien date.

RECOMMENDATION 9: Assess private water company property at the lower of market value or factored base year value.

In our prior survey we suggested that the assessor revise his approach to assessing private water companies regulated by the California Public Utilities Commission. The assessor's practice has been to enroll factored base year value, adjusted for additions or deletions after the base year. Because this amount exceeded HCLD, which was the basis for rates charged to customers, private water companies may have been assessed at values higher than market levels. Our review of water company appraisal records during our current survey showed that this practice continues.

HCLD is a valid indicator of market value for private water companies when regulation restricts earnings of the water company to a certain percentage of a rate base which approximates HCLD. The HCLD should be adjusted for licensed vehicles and other nontaxable items.

While HCLD is an important indicator of value for regulated water companies, we do not suggest that it should be the only indicator of value used in determining a company's current market value. HCLD is an important indicator only to the extent that potential buyers and sellers of water companies are influenced by CPUC regulations. Sales and income approaches may indicate that market value is higher or lower than HCLD. We encourage the assessor to consider the sales comparison and income approaches to value in addition to HCLD when information is available.

C. SPECIAL ASSESSMENT PROCEDURES

1. Supplemental Assessments

We reviewed the section on supplemental assessments in the Humboldt County assessor's procedures manual and also selected appraisal files for compliance with the provisions of Revenue and Taxation Code sections 75 through 75.80. These code sections pertain to supplemental assessments for change in ownership and new construction events. It appears that the assessor's staff is enrolling supplemental assessments properly and timely. However, we found, as we did in our 1990 assessment practices survey of Humboldt County, that the county auditor is still not notified of some possible supplemental assessments as required by Revenue and Taxation Code section 75.30 which directs the assessor and auditor as follows:

“...Whenever the assessor determines that a change in ownership or the completion of new construction has occurred, the assessor shall place a notice of pending supplemental billing on the roll being prepared and shall notify the auditor, who shall place a notation on the current roll or on a separate document accompanying the current roll that a supplemental billing may be forthcoming.”

RECOMMENDATION 10: Notify the county auditor of possible supplemental assessments caused by new construction.

The assessor maintains a computer program which stores a list of pending reappraisals caused by changes in ownership. The county auditor uses this computerized list to place a notation on the current roll and the roll being prepared which states that a supplemental billing may be forthcoming.

As we discussed in our prior survey report, this roll update feature is limited to changes in ownership; there is no such provision for assessable new construction. Therefore, no notation appears on the rolls regarding supplemental assessments due to assessable new construction.

The assessor is complying with section 75.30 for all properties with a change in ownership, but not for properties having assessable new construction. Although supplemental assessments are levied for new construction, there is no notation of the assessment placed on the

roll. We again recommend that the assessor develop a computer program for new construction supplemental assessments similar to the one used for tracking change in ownership supplemental assessments.

2. Declines in Value

California property tax law requires the assessor to assess most real property each year at the lower of its current market value or its factored base year value. During the recent economic decline, many California assessors have been deluged with requests by taxpayers for reductions of their assessments. However, this has not been a major problem in Humboldt County.

The assessor's staff indicated to us that while property values may have stabilized in most areas of Humboldt County, few noticeable declines in value have occurred. There were 110 properties on the 1996-97 roll for which the assessor's staff recognized declining values; this is up from 104 in 1995-96. Among these, most were either shopping centers (malls), motels, residential property in Shelter Cove, or wood product manufacturing plants.

Parcels that the assessor's staff determines to have declined in value are reviewed annually until the factored base year value once again becomes the basis for assessment. We determined that the staff made appropriate adjustments upon discovery of the declines, with the exception of wood product manufacturing plants. The determination of market value for these plants is based on an inappropriate definition of the appraisal unit; the issue is discussed in the business property section of this report.

IV. PERSONAL PROPERTY VALUATION AND ASSESSMENT

A. INTRODUCTION

The Humboldt County Assessor's personal property and business fixtures appraisal staff consists of four auditor-appraisers, one appraisal technician, and two assessment technicians who are responsible for 8,119 personal property and fixture assessments. This includes: 4,562 commercial, industrial, or agricultural properties, 204 aircraft (including 3 certificated aircraft), 2,553 boats, and 800 field appraisals.

The BOE's sampling of the 1992-93 assessment roll included 91 secured and unsecured personal property and fixture assessments. In 62 of these items, the assessor's value differed from the value determined by the BOE staff. Specifically, the local roll value exceeded the BOE staff's values on 32 items, and on 30 items the BOE staff's value was higher. Fifteen sample items involved problems with either underreporting or non-reporting. Value differences noted in two other sample items were caused by differences in the classification of business property by BOE staff and assessor's staff. The remaining value differences were caused by procedural exceptions, varying appraisal judgments, and other areas of disagreement between BOE and assessor staffs. We did not find that these remaining differences indicated any major program deficiencies.

The assessor is still working to obtain a computer system and programs that would relieve the staff from much of the manual processing and computation that consumes much of their time. Having their own computer system would also allow the assessor's staff to keep a four-year history of all mandatory audit accounts, and prepare an annual listing, including a four-year history of penal assessments, as we suggested our last survey report.

The assessor has been doing a good job of keeping abreast of the personal property and business fixtures assessment program. He has made a significant effort to implement prior survey recommendations and suggestions that he believed would improve the assessment program and for which he had budget. He implemented the following four of our prior survey recommendations or suggestions: (1) annually appraise pleasure boats at market value; (2) do not assess equipment mounted on licensed vehicles; (3) enhance screening for signatures on property statements; and (4) insure that value changes are completely documented in the appraisal file. Our prior suggestion to "Use clerical personnel to process most business property statements" has been partially implemented. One appraisal technician and two assessment technicians assist in processing business property statements, but the four auditor-appraisers in the office still spend much of their time processing property statements.

As mentioned earlier, some recommendations and suggestions were not implemented due to budgetary problems, or because the assessor did not agree with their importance. However, we believe most are important enough to repeat. The recommendations and suggestions set forth in this survey report, if implemented, would improve the operation of the assessor's personal property and business fixtures assessment program.

B. BUSINESS PROPERTY VALUATION AND ASSESSMENT

1. Property Statement Processing

The assessor sends out over 5,000 business property statements annually, which should be the basis for assessments. Instead, property values are calculated using the assessor's equipment appraisal sheet created from the prior year's property statements. Costs and market values are updated beginning in July or August of any given year; property statements are not received until February or March of the following year. When the property statements are received, there is an attempt to update the assessor's equipment appraisal sheets by adding the reported additions and by deleting the reported disposals. The results have many inaccuracies as demonstrated by the numerous adjustments made when an audit is conducted.

Our review disclosed the following problems in processing property statements and calculating assessed values:

- (1) use of the assessor's Equipment Appraisal Sheet instead of the submitted property statement results in too many assessment errors. Virtually all 18 audits that we reviewed had under or over assessments due to errors in the Equipment Appraisal Sheets used by the assessor;
- (2) use of improper replacement cost new (RCN) trend and percent good factors may result in erroneous valuations. The assessor's staff extrapolates RCN trend and depreciation factors well before information is available for the prospective lien date;
- (3) costs reported by the taxpayer are not audited. The assessor's audit is used to confirm the accuracy of the equipment appraisal sheets; property is either added to or deleted from this list;
- (4) incomplete cross checking of business property statements may result in escapes or double assessments because the same property may be reported by different taxpayers; and
- (5) real property additions (new construction) are not as likely to be enrolled.

RECOMMENDATION 11: Revise business property valuation procedures by: (1) assessing property based on reported costs on annual business property statements; (2) using cost indices and percent good factors that are contemporaneous with the current lien date; and (3) discontinuing the practice of limiting the percent good in depreciation tables to an arbitrary minimum level.

Assess Property Based On Reported Costs On Annual Business Property Statements

The previous survey report recommended that the assessor immediately stop using equipment appraisal sheets and calculate equipment values in the space provided on the property statements. The assessor's equipment appraisal sheet system requires the auditor-appraiser to extend the values separately for each item acquired in a single year, which is a time consuming

method of computing depreciated replacement cost new. The time saved by implementing this processing technique could be used to increase audit production. The property statement instructs the taxpayer to group equipment into one of a small number of categories and list its cost and year of acquisition. The major advantages are speed and accuracy; in most cases, it requires only a few minutes to estimate the replacement cost for all equipment reported for an account. Numerous clerical errors occur as a result of the system the assessor's staff uses to assess business property. Additional time is lost in making changes to the equipment lists and to roll changes.

The assessor has not implemented the previous recommendation, but neither has he received the much anticipated computer or software that would allow him to make beneficial changes. We again recommend that the assessor assess property based on reported costs on annual business property statements

Cost Indices And Percent Good Factors

In the cost approach to value, market values are estimated by applying an index factor to the acquisition cost to arrive at an estimate of replacement cost new. Depreciation is recognized by applying a percent good factor to this replacement cost new estimate to estimate market value.

The assessor's staff updates business property assessment records and estimates market values for the prospective lien date for business properties in the period from July 1 to the lien date each year. In order to accomplish the activity at that time of year, the supervising auditor-appraiser estimates months in advance of the prospective lien date what the RCN index and percent good factors will be for the prospective lien date valuation activity. The assessor's factors overestimate the value of equipment when compared to the use of the BOE's equipment index and percent good factors which are updated annually in the Assessors' Handbook (AH) Section 581, Equipment Index Factors.

The assessor should use each lien date's edition of AH 581 when it becomes available; this would eliminate the practice of using improper indices and factors. We recommend the assessor use RCN indices and percent good factors that are applicable to the lien date for each assessment roll.

Discontinue The Practice Of Limiting The Percent Good In Depreciation Tables To An Arbitrary Minimum Level

This was a recommendation in the prior survey. The assessor should discontinue this practice because it creates assessments that exceed market value. Review of our sample appraisals indicated that for many samples this practice caused the assessor's values to be higher than CPTD's.

The BOE annually publishes Assessors' Handbook Section 581 to help assessors in the valuation of business personal property and business fixtures. The percent good factors

contained in the handbook are based on a logical premise that these types of properties lose value as they age. The calculation of the percent good factors is consistent with generally accepted appraisal practices. The percent good factors are intended to reflect the average loss in value that commercial and industrial properties of these types will generally suffer over a period of time.

When valuing property, it is necessary for appraisers to analyze individual property items for deviations from the norm. If such deviations exist, it is appropriate to adjust the normal percent good factors to reflect the deviation. However, arbitrary deviations from the normal percent good, such as establishing minimum percents good, are not acceptable appraisal practices. The Humboldt County Assessor has stated that he believes that his policy better reflects the actual marketplace, however he does not have any studies or data to support this contention. We recommend that the assessor discontinue the practice of limiting the minimum percent good in depreciation tables to an arbitrary level.

2. Computers

The valuation of computers and related equipment (herein referred to as computers) has been a contested issue between taxpayers and assessors for the last few years. In its continuing effort to maintain proper, equitable, and uniform property tax assessments, the BOE, in Letter to Assessors (LTA) 95/26, dated April 5, 1995, recommended valuation factors for assessors to use when valuing non-production computers for the 1995 lien date.

For the 1996 lien date, the BOE issued LTA 96/19, dated March 6, 1996, which contained tables for personal and mainframe computers. Letter to Assessors 96/27, dated April 3, 1996, expanded these two tables into three tables, i.e. personal (\$25,000 or less), mid-range (\$25,000 to \$499,000), and mainframe (\$500,000 or more). These new tables contained factors that were developed after consultation with the computer industry and the county assessors. Letter to Assessors 96/27 also states that the BOE staff had been instructed to continue acquiring and analyzing data for the mid-range table. No additional data, other than that available for LTA 95/26, was incorporated into the mid-range table that was set forth in LTA 96/27. However, it is the BOE's position that the proper application of the factors would yield a reasonable estimate of the current market value of computers for the 1996 lien date.

RECOMMENDATION 12: Assess computers by using the BOE's recommended factors.

The assessor is not using the BOE's recommended factors in valuing computers. A review of the assessment of the largest lessor of computer equipment in Humboldt County revealed that the assessor may have overvalued this equipment by more than \$192,000. This equates to 184 percent of the value that would have been assessed if the BOE's computer tables had been used. The assessor valued the equipment using the factors from his tables despite the fact that the taxpayer had attached computer value computations to the property statement based on the information contained in the LTA's. Copies of the LTA's were also attached to the business property statement submitted to the assessor.

The BOE's computer factors were developed after extensive data-gathering, analysis, and consultation with the computer industry and assessors. Use of different valuation factors is contrary to the BOE's guidelines, and results in an assessment practice other than that recommended by the BOE.

We recommend that the assessor assess all computers by applying the factors recommended in the BOE's LTA 96/27.

3. Proper Appraisal Unit

Recognizing a decline in market value below factored base year value for real property assessments is required by Revenue and Taxation Code section 51 and California Code of Regulations, Title 18, Public Revenues, Division 1, Property Tax Rule 461. Proper application of this concept requires a correct definition of the appraisal unit; Rule 461(d) specifies that fixtures are to be considered a separate appraisal unit when evaluating property for a decline in value below factored base year value.

RECOMMENDATION 13: Comply with Property Tax Rule 461(d) when determining the proper appraisal unit for determination of taxable value; enroll the lower of the factored base year value or the current market value as the taxable value of each appraisal unit.

Our review of the assessment of a major wood products plant revealed that while the assessor's staff is recognizing declines in value below factored base year for the total property, their computations to arrive at a current market value, and their allocations to the various appraisal units and property classes were incorrect. The assessor's current market value of the total property, which included land, land improvements, structures, fixed machinery and equipment classified as improvements, and personal property, was determined by the income approach to value. This current market value of the total property was then averaged with the sum of the factored base year values of land and improvements plus the current market value of fixtures. The result was the current taxable value estimate of the property. The current market value was not allocated to the individual appraisal units contained in the total property in order to compare the factored base year value of each appraisal unit to the unit's current market value as required by Property Tax Rule 461(d).

For the cable television possessory interest assessment in Eureka, the assessor's staff does not make a comparison of current market value and factored base year value when determining taxable value. Instead they add, to the factored base year value, the current market value of new subscribers to the system and enroll that result as the taxable value.

This hybrid method of assessing the cable TV possessory interest is incorrect. New subscribers are not necessarily the result of new construction nor or they necessarily indicative of an expansion of the possessory interest. A determination must be made as to whether or not the new subscribers result from new cable extensions, added services from existing cable lines, or an expansion of the possessory interest territory. New cable extensions or

an expansion of the possessory interest territory should be enrolled at a new base year value. Additional subscribers to existing property do not create additional assessable value. Also the market value created by additional subscribers should be allocated to each of the business enterprise's appraisal units in order to determine each unit's market value for determination of taxable value pursuant to Revenue and Taxation Code section 51.

In these two instances the assessment methods used by the assessor's staff ignore the requirement of Rule 461(d) to ascertain the fair market value of each appraisal unit and compare the fair market value to the factored base year value of that appraisal unit in order to determine taxable value. The rule recognizes that a business enterprise may have three appraisal units at a location. These potential appraisal units are land and structures, fixtures or other machinery and equipment classified as improvements, and personal property. Each group is a separate appraisal unit, even though they might be part of the same business enterprise.

For real property, the assessed value should be each appraisal unit's factored base year value or current market value, whichever is lower. The market value of the personal property is an additional assessment. Letter to Assessors 79/39, Real Property Value Changes, states that declines in value in one appraisal unit cannot be offset by increases in land and improvement values in another appraisal unit. Therefore, after allocation of current market value to the proper appraisal units, the assessor must enroll the lower of market value or factored base year value of each appraisal unit.

We recommend the assessor's staff follow Rule 461(d) when determining the proper appraisal units for evaluating real property assessments for declines in value below factored base year value.

C. AUDIT PROGRAM

The prior two survey reports rated the Humboldt County Assessor's audit program as being "very effective." In terms of timeliness and productivity we found this to still be the case. However, our following suggestion, if implemented, could improve audit quality.

SUGGESTION 5: Develop a more comprehensive audit program by: (1) maintaining a record of mandatory accounts with a four-year history of assessment amounts; (2) formalizing a nonmandatory audit program; and (3) using an audit checklist and a comprehensive audit narrative in every audit.

Record Of Mandatory Audits

The mandatory audit program is an important function of the business property assessment program in any assessor's office. Revenue and Taxation Code section 469 requires that the financial records of businesses that own, claim, possess, or control trade fixtures or business tangible personal property with a full value of \$300,000 be audited at least once every four years. The California Code of Regulations, Title 18, Public Revenues, Division 1, Rule 192

clarifies the audit requirement to mean that the minimum value has to have been achieved in each of four consecutive years.

In our prior survey report, we made a suggestion to expand the computer listing of mandatory accounts to include a four year history. This suggestion was made in order to identify those accounts that meet the criteria for a mandatory audit. Currently the assessor does not have an exclusive listing of mandatory audit accounts. The computerized list used by the assessor's staff includes all accounts with property valued in excess of \$100,000 for one year, and problem accounts (including taxpayers who fail to file property statements for one or more years). The list does not indicate how many years the taxpayer had property at the mandatory audit level. A manually maintained list, produced by the assessor's staff, records accounts selected for audit for the upcoming fiscal year. This record currently indicated 364 audits to be performed during a four year cycle.

The assessor should develop a comprehensive listing to track accounts that meet the mandatory audit criteria. A comprehensive listing would assist the assessor's staff in determining when these mandatory audit accounts are due for audit. This would assist in the effort to audit all accounts within the four year period required by Revenue and Taxation Code section 469.¹ The list should provide the taxpayer's name, account number, parcel numbers involved, address, history of assessed value for the last four years, date of last audit, when next audit is scheduled, results of last audit, location of books and records, and audit contact. Once this data is available, the assessor's staff may use it as an administrative tool in scheduling audits by state, city, or zip code area.

We suggest that the assessor prepare an audit log of mandatory accounts with a four-year history of the assessment amounts.

Formalize A Nonmandatory Audit Program

In Humboldt County few audits have been conducted on the property of owners whose assessments do not meet the criteria for a mandatory audit as expressed in Revenue and Taxation Code section 469. In the 1995-96 audit year only five nonmandatory accounts were audited; in the 1994-95 audit year only eight such accounts were audited; the amounts of escape assessments enrolled as a result of these activities were minimal. Twenty nine accounts were audited for the 1993-94 tax year resulting in \$1,304,626 in value being enrolled as escape assessments. In the 1992-93 audit year \$2,252,386 in value was enrolled as a result of the nonmandatory audit activities.²

Although no legal requirement exists to audit small accounts, no auditing program is complete unless it includes a representative sampling from all sizes and types of accounts, including those that do not meet the mandatory audit level. A major objective of an audit

¹ Our review of over 30 audits did not find that any were conducted outside the four-year time frame mentioned in R & T Code section 469, but since the audit log did not detail all that were eligible for audit, using the \$300,000 limit for four years, we could not be sure that all were done timely.

² Statistics are from a report titled "NUMBER OF AUDITS PERFORMED AND AMOUNTS OF RECAPTURE."

program is to encourage proper reporting on the annual business property statements. In addition, the objective of an audit selection system should be selection of those accounts for audit which will produce tax revenue changes equal to or greater than the cost of auditing. For example, in selecting accounts to audit, the assessor's first choice should be the account where a value change is likely to occur. Those accounts showing little or no likelihood of value changes should be considered low priority for audits.

Taxpayer underreporting on the annual business property statement is a significant problem in practically every assessor's office in California. Some of this underreporting would be reduced with a more intensive nonmandatory audit program. We suggest the business property section establish an audit selection criteria for nonmandatory accounts and implement a formal nonmandatory audit program as soon as possible.

Require The Use Of An Audit Checklist And An Audit Narrative In Every Audit

In our prior survey we suggested that the assessor's staff increase audit documentation. We also suggested that the audit narrative include a statement to the effect that the auditor reviewed the ownership of the legal entity for potential change in ownership events. Our current review of over 30 audits does indicate increased documentation by the audit staff, and the audit reports lack an audit checklist and a comprehensive audit narrative.³ There was no statement relating to a review of potential change in ownership in any of the audit narratives that we reviewed.

Audits verify the data submitted on the annual property statement and follow certain general steps to ascertain the validity of reported figures and other information. A checklist details the pertinent points covered during the audit. The checklist, along with the audit narrative, provides valuable information for further questions, audit review, and future audit preparation.

The audit narrative has been described as "a summary of findings." It should contain: (1) findings; (2) conclusions as a result of the findings; (3) opinion and reason for any change made to the original assessment; and (4) recommendations for or against penalties. The narrative should logically follow the sequence of the working papers contained in the audit. It should cover significant points in enough detail so that a reviewer can reach a conclusion as to the adequacy of the audit. All areas covered in the audit should be listed even if there were no cost or valuation differences. If no cost or valuation differences for an audit topic were discovered during the audit, a simple "no cost or valuation differences were noted" statement would suffice.

We suggest that the assessor require the use of an audit checklist and a comprehensive audit narrative in every audit.

³ None of the thirty audits reviewed contained an audit checklist; two did not contain an audit narrative; the rest contained narratives that were considered brief or adequate.

SUGGESTION 6: Improve audits by including the following topics in audits when appropriate: (1) flight and ground time for commercial airline companies; (2) income and expense data when it is used to value the property; and (3) interest during construction on large commercial and industrial properties.

Flight And Ground Time

Audits of two commercial airline companies that serve Humboldt County produced escaped assessments due to underreporting of costs or values of aircraft. However, the flight and ground time and arrivals and departures used in the allocation formula to assess commercial carriers were not audited. This information is critical in determining the airline companies' assessments.

Revenue and Taxation Code section 1152 explains the allocation formula to be used by California assessors when assessing certificated aircraft. When airline companies file their business property statements, they must submit a supplemental schedule titled Air Carrier's Operation Report. When an audit is conducted, all the information on this report should be audited. We suggest that the assessor examine flight and ground time information in future audits.

Income And Expense Data

Annually, income and expense data is submitted by a major manufacturer in Humboldt County for use by the assessor in valuing its property. The use of the income approach has resulted in a lower property value for the taxpayer. The assessor's staff routinely uses this unaudited income and expense data to value this taxpayer's property. This data should be examined when an audit is conducted. We suggest that the assessor and his staff audit income and expense data when it is used to value property.

Interest During Construction.

None of the audits of commercial or industrial properties we reviewed mentioned that interest on funds used for construction was capitalized on major construction projects, or that such interest was imputed as part of the value estimate of such projects. Several of the larger industrial plants doing business in Humboldt County constructed replacement plant or new additions costing millions of dollars (one project was more than \$50 million). The addition of construction period interest to the value estimate might have added millions of dollars to the assessment if it was not included in the reported costs.

The California Code of Regulations, Title 18, Division 1, Rule 6, *The Reproduction And Replacement Cost Approaches to Value*, under subsection (b), provides, in part:

“...The reproduction cost of a reproducible property...may be estimated by... (2) applying current prices to the property's labor

and material components with appropriate additions for entrepreneurial services, interest on borrowed or owner supplied funds...” (emphasis added).

The audit work papers of the assessor’s staff neither document the review of costs for inclusion of construction period interest nor its inclusion in the value estimate. We suggest the assessor audit for these costs and document when they have been reported, or that interest on funds used during construction has been included in the value estimate.

D. OTHER TAXABLE PERSONAL PROPERTY VALUATION AND ASSESSMENT

1. Vessel Valuation

Humboldt County has an extensive coastline on the Pacific Ocean with a fine harbor. There are 8,654 boats on the unsecured property tax roll for 1996, the majority of which are pleasure boats. The county values the boats at market value each year with the aid of two value guides, the ABOS, New Boat & Motor Price Guide Blue Book and BUC Used Boat Price Guide. The county exempts low-valued boats if the market value is below \$2,000 as authorized by Revenue and Taxation Code section 155.20.

The assessor has an effective discovery program for boats new to their county. The boats are tracked through reports from the Department of Motor Vehicles (DMV), and referrals from other counties of boat owners moving with their boats to Humboldt County. Additionally, the Coast Guard annually sends a list to the assessor of all the boats of which the Coast Guard is aware. The Harbor Master at the Humboldt Bay Harbor District sends a statement on BOE Form AH 576C, which identifies each boat in the harbor.

RECOMMENDATION 14: Assign a certified appraiser the responsibility of determining boat values.

Currently the valuation of boats and vessels is assigned to an appraisal technician, who is doing a commendable job. However, Revenue and Taxation Code section 670 states that no person shall perform the duties or exercise the authority of an appraiser for property tax purposes as an employee of the state, any county or city and county, or city, either general law or chartered, unless they are the holder of a valid appraiser’s or advanced appraiser’s certificate issued by the State Board of Equalization. The appraisal technician who values boats does not hold an appraiser certification. We recommend that a certified appraiser review the appraisal technician’s value estimates and accept responsibility for the value estimates.

2. Aircraft Valuation

The assessor’s staff does a commendable job of discovering and assessing aircraft in their county by using listings from the Federal Aviation Agency (FAA) and airport manager reporting on the List of Aircraft, BOE Form AH 577B. The assessor also receives referrals about aircraft from other counties. Field canvassing is not used to locate aircraft. Certificated aircraft

are discovered through business property statements and by checking the yellow pages of the local telephone directory for a list of commercial airlines operating in the county.

The value for any given airplane is likely to be substantially different from the value suggested in published aircraft value guides. Values vary depending on the overall condition, the equipment installed, the hours since major overhaul, and the total hours on the airplane and engine(s). The values of newer aircraft are most affected by the presence or lack of optional equipment, while the values of older aircraft are influenced more by the condition of the aircraft.

Our previous survey report recommended that the assessor make engine hour adjustments when appraising private aircraft. The assessor's staff has complied with this suggestion by acquiring a computer program designed for the appraisal of aircraft. The program, "Software for the Aircraft Bluebook," has been a very effective tool for the assessor's office. The program requires information about the model of aircraft and additional information for a computerized worksheet that calculates retail and wholesale pricing for an aircraft. The worksheet may be printed or saved off-line. The worksheet allows for editing the aircraft name, engine hours, serial number, registration number, and information for additions and deductions based on features and condition of the aircraft. The program uses this information to calculate an estimate of value.

Humboldt County has two historical aircraft in the county. The assessor's office receives all affidavits for exemption for historical aircraft by 5:00 p.m. on April 1 of each year. There has never been an instance of any taxpayer filing after April 1. The \$35 application fee is collected with the initial filing for the exemption and is not collected yearly. The assessor's staff does not verify the 12 occasions of public display required for the historical aircraft exemption.

Our review of 23 randomly selected and various types of aircraft assessment indicates that the assessor's staff is doing a good job of assessing aircraft.

3. Manufactured Homes

A property item described in Health and Safety Code sections 18007 and 18008 as a manufactured home/mobile home (MH) is defined, for property tax assessment purposes, in Revenue and Taxation Code section 5801 as personal property if the MH is not on a permanent foundation. If the MH is on a permanent foundation, section 5801 defines it as real property which precludes it from characterization as a MH for property tax assessment purposes.

Revenue and Code sections 5801, et seq. is a self contained section of law which recreates the principles of Article XIII A of the California Constitution for the assessment of MH's. Although a MH must be classified as personal property, most of the provisions relating to the taxation of other personal property are not applicable. The primary differences in the taxation of MH's from other items of personal property are: (1) the assessment of a MH is entered on the secured roll; (2) the taxes on a MH may be paid in two installments; (3) a base year value is determined for a MH on the date it changes ownership or undergoes new construction; (4) the

base year value is compounded annually by an inflation factor; (5) the taxable value of a MH is the lesser of its factored base year value or its full cash value on the lien date taking into account reductions in value due to any factor causing a decline in value while other items of personal property are assessed at full cash value without the upper limit of a factored base year value and (6) a MH which undergoes a change in ownership or new construction is subject to supplemental assessment.

For the 1996-97 fiscal year Humboldt County had a total of 5,863 MH's located within the county boundaries. Of this total 2,235 were considered subject to ad valorem property taxation. Most of these taxable MH's are located in the 37 manufactured home parks scattered throughout the county. In the Humboldt County Assessor's Office, the responsibility for valuing these units is as follows: (1) all MH's located within the MH parks are assigned to one appraiser and (2) those located outside the parks are assigned to the individual appraiser responsible for the areas in which they are located.

In our review of the county's records, we selected and examined the appraisal records of all MH's located in three of the 37 MH parks located in Humboldt County. In addition to these three MH parks, we also examined the records of 38 MH's assessed with a land parcel. This review resulted in the following recommendations.

RECOMMENDATION 15: Revise manufactured home assessments by: (1) classifying assessable manufactured homes on non-permanent foundations as personal property on the secured assessment roll; (2) enrolling the lower of the factored base year value or the current market value as the taxable value of all assessable manufactured homes; and (3) not applying the Article XIII A inflation factor to a prior year's market value estimate.

Classify Manufactured Homes As Personal Property On The Secured Assessment Roll

The assessor's staff currently classifies all MH's subject to property tax as real property. In many situations this misclassification will not affect the actual amount of taxes levied. However, if the MH classified as real property is within a tax rate area that has special assessments, its owner may be assessed unauthorized taxes unless the county auditor has a method of identifying the MH assessment as an assessment against personal property. The unauthorized taxes would be the special assessments that are levies only upon real property for various purposes. Humboldt County had approximately 33 special assessment districts levying fees for fire, water, and sewer maintenance services.

We recommend that the assessor classify MH's subject to ad valorem property tax as personal property.

Enroll The Lower Of The Factored Base Year Value Or The Current Market Value

Our examination of the MH assessment records disclosed that adjustments for a market value lower than factored base year value are mostly made upon request. In a few instances values are reduced when sales in an area indicate declining values. There is little attempt to apply these adjustments uniformly throughout the county or on an annual basis. Real property values in many areas of California have declined or remained stagnant for a number of years. Even during periods of increases in real property values, the values of many MH's may decrease below their factored base year values. Revenue and Taxation Code section 5813 requires that the taxable value of MH's shall be the lower of the factored base year value or the current market value.

In our examination of those records in which decline in value adjustments were made, we found that, overall, the county's adjustments were generally based on good market data. The appraiser responsible for the assessments of manufactured homes located in manufactured home parks has maintained a very good market data bank for sales of manufactured homes sold throughout the county. Besides this data, the assessor's staff utilizes a periodic listing from the Department of Housing and Community Development (HCD) showing sales of new units, resales, changes of situs, and voluntary conversions from vehicle license fee status to local property taxation. Additionally the assessor's staff relies on a replacement cost less depreciation estimate based on cost factors supplied by the BOE's Policy, Planning, and Standards Division. They do not rely on recognized value guides for valuing MH's.

We recommend that the Humboldt County assessor's staff develop a program to annually compare and enroll the lower of the factored base year value or the current market value of all assessable MH's.

Do Not Apply The Article XIII A Inflation Factor To A Prior Year's Market Value Estimate

For a MH with a taxable value lower than factored base year value, the current practice of the assessor's staff is to factor that prior year's taxable value by the Article XIII A inflation factor until such time as the result equals or exceeds the factored base year value. At that point the factored base year value resumes as the taxable value.

The Article XIII A inflation factor should only be applied to a base year value. It should not be applied to a prior year's taxable value that represented a market value that was less than the factored base year value. Each year's market value estimate should be made as an independent judgment and not as the result of factoring a prior year's taxable value for inflation.

We recommend that the Humboldt County assessor's staff stop applying inflation factors to prior year's taxable values.

4. Animals

Certain types of horses are the only animals that are subject to property taxation, other animals are either exempt as household pets or as the result of a business inventory exemption. As is the case in most counties, taxation of horses is a very minor part of the

assessor's duties. The assessor's staff acquires information about taxable horses from newspapers, stud service advertisements, and breeders. The staff accepts the owner's statement that horses or other animals are pets and are not held for commercial purposes or as investments.

Racehorses are subject to the special taxation procedures specified in Revenue and Taxation Code sections 5701 through 5790. The assessor's duty under these statutes is to identify the owners of racehorses and to furnish the owners with an annual report to be filed by the owners and to audit those reports.

Humboldt County has three racehorses, and they are owned by the same taxpayer. The assessor's office mails out the Annual Racehorse Tax Return form (AH 571-J) to the taxpayer and the taxpayer returns the form with the tax payment to the tax collector. The tax collector sends copies of the check and the tax return to the assessor's office for retention for five years. The total county-wide racehorse tax liability for 1996 was \$108.

There are five other taxpayers who own taxable horses, including Arabian horses and pack mules. The taxpayers report these animals on the Registered and Show Horses Other Than Racehorses form (AH 571-F-2).

Our research on this topic indicates the assessor's staff is aware of their responsibility regarding taxation of animals and makes a reasonable effort to fulfill that responsibility.

THE ASSESSMENT SAMPLING PROGRAM

The need for compliance with the laws, rules, and regulations governing the property tax system and related assessing¹ activities is very important in today's fiscally stringent times. The importance of compliance is twofold. First, the statewide maximum tax rate is set at 1 percent of taxable value. Therefore, a reduction of local revenues occurs in direct proportion to any under valuation of property. (It is not legally allowable to raise the tax rate to compensate for increased revenue needs.) Secondly, with a major portion of every property tax dollar statewide going to public schools, a reduction in available local property tax revenues has a direct impact on the State's General Fund, which must backfill any property tax shortfall.

The BOE, in order to meet its constitutional and statutory obligations, focuses the assessment sampling program on a determination of the full value of locally taxable property and eventually its assessment level. The purpose of the BOE's assessment sampling program is to review a representative sampling of the assessments making up the local assessment rolls, both secured and unsecured, to determine how effectively the assessor is identifying those properties subject to revaluation and how well he/she is performing the valuation function.

The assessment sampling program is conducted by the BOE's County Property Tax Division (CPTD) on a five-year cycle for the 11 largest counties and cities and counties and on either a random or as-needed basis for the other 47 counties. This sampling program is described as follows:

- (1) A representative random sampling is drawn from both the secured and unsecured local assessment rolls for the county to be sampled.
- (2) These assessments are stratified into 18 value strata (nine secured and nine unsecured).²
- (3) From each stratum a random sampling is drawn for field investigation, sufficient in size to reflect the assessment level within the county.
- (4) For purposes of analysis, the items will be identified and placed into one of the following five categories after the sample is drawn:

¹The term "assessing" as used here includes the actions of local assessment appeals boards, the boards of supervisors when acting as boards of equalization, and local officials who are directed by law to provide assessment-related information.

²The nine value strata are \$1 to \$99,999; \$100,000 to \$199,999; \$200,000 to \$499,999; \$500,000 to \$999,999; \$1,000,000 to \$1,999,999; \$2,000,000 to \$19,999,999; \$20,000,000 to \$99,999,999; \$100,000,000 to \$249,999,999; and \$250,000,000 and over.

- a. “B” (base year) properties. Those properties the county assessor has not revalued for either an ownership change or new construction during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling.
 - b. “T” (transferred) properties. Those properties last revalued because of an ownership change that occurred during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling.
 - c. “C” (new construction) properties. Those properties last revalued to reflect new construction that occurred during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling.
 - d. “N” (non-Proposition 13) properties. Those properties not subject to the value restrictions of XIII A, or those properties that have a unique treatment. Such properties include mineral-producing property, open-space property, timber preserve property, and taxable government-owned property.
 - e. “U” (unsecured) properties. Those properties on the unsecured roll.
- (5) From the assessment universe in each of these 18 value strata (nine strata on both secured and unsecured local rolls), a simple random sampling is drawn for field investigation which is sufficient in size to reflect the assessment practices within the county. A simple unstratified random sampling would cause the sample items to be concentrated in those areas with the largest number of properties and might not adequately represent all assessments of various types and values. Because a separate sample is drawn from each stratum, the number of sample items from each category is not in the same proportion to the number of assessments in each category. This method of sample selection causes the raw sample, i.e., the "unexpanded" sample, to over represent some assessment types and under represent others. This apparent distortion in the raw sampling is eliminated by "expanding" the sample data; that is, the sample data in each stratum are multiplied by the ratio of the number of assessments in the particular stratum to the number of sample items selected from the stratum.

Once the raw sampling data are expanded, the findings are proportional to the actual assessments on the assessment roll. Without this adjustment, the raw sampling would represent a distorted picture of the assessment practices. This expansion further converts the sampling results into a magnitude representative of the total assessed value in the county.

- (6) The field investigation objectives are somewhat different in each category, for example:
- a. Base year properties -- for those properties not revalued during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling: was the value properly factored forward (for the allowed inflation adjustment) to the roll being sampled? was there a change in ownership? was there new construction? or was there a decline in value?
 - b. Transferred properties -- for those properties where a change in ownership was the most recent assessment activity during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling: do we concur that a reappraisal was needed? do we concur with the county assessor's new value? was the base year value trended forward (for the allowed inflation adjustment)? was there a subsequent ownership change? was there subsequent new construction? was there a decline in value?
 - c. New construction -- for those properties where the most recent assessment activity was new construction added during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling: do we concur that the construction caused a reappraisal? do we concur with the value enrolled? was the base year amount trended forward properly (for the allowed inflation adjustment)? was there subsequent new construction? or was there a decline in value?
 - d. Non-Prop 13 properties -- for properties not covered by the value restrictions of Article XIII A, or those properties that have a unique treatment, do we concur with the amount enrolled?

- e. Unsecured properties -- for assessments enrolled on the unsecured roll, do we concur with the amount enrolled?
- (7) The results of the field investigations are reported to the county assessor, and conferences are held to review individual sample items whenever the county assessor disagrees with the conclusions.
- (8) The results of the sample are then expanded as described in (5) above. The expanded results are summarized according to the five assessment categories and by property type and are made available to the assessment practices survey team prior to the commencement of the survey.

The primary use of the assessment sampling is to determine an assessor's eligibility for the cost reimbursement authorized by Revenue and Taxation Code section 75.60. During the course of the sampling activity, the assessment practices survey team may also discover recurring causes for the differences in the opinion of taxable value that arise between the assessor and the County Property Tax Division. These discoveries may lead to recommendations in the survey report that would not have otherwise been made.

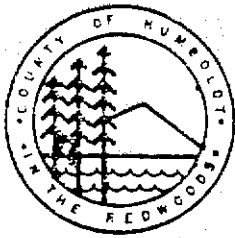
ASSESSOR'S

RESPONSE

TO

BOARD'S

RECOMMENDATIONS



COUNTY ASSESSOR
COUNTY OF HUMBOLDT

825 5TH STREET
EUREKA, CALIFORNIA 95501 PHONE (707) 445-7276

May 29, 1998

RECEIVED
JUN 01 1998
County Property Tax Division
State Board of Equalization

Mr. William B. Jackson, Chief
County Property Tax Division
Department of Property Taxes
California State Board of Equalization
450 N Street, MIC: 62, 21st Floor
P.O. Box 942879
Sacramento, CA 94279-0062

Dear Bill:

Enclosed is my Response to your survey of this office in accordance with Section 15645 of the California Government Code.

The sampling of the 1992-93 Humboldt County assessment roll showed that Humboldt County was within the legal and statistical limits required by California Revenue and Taxation Code Section 75.60. The high level of quality of the Humboldt County assessment roll and assessment program is the direct result of the efforts of the staff in this office. These employees do an outstanding job for the property owners of Humboldt County.

You will note in my Response that I concur with many of the recommendations, but there are some with which I do not agree for various reasons.

To the Appraisal Team Director, J. Thomas McClaskey, the Survey Team Supervisor, David J. Hendrick, and their team members, I wish to express my appreciation. They performed the sampling and survey with a minimum of disruption and in a professional manner.

Finally, to the employees of the Humboldt County Assessor's Office I want to express my thanks for their dedicated efforts in putting out an excellent assessment roll year after year.

Sincerely,

Raymond L. Jerland, Assessor

RLJ/jh

RESPONSE TO RECOMMENDATIONS

RECOMMENDATION 1: *Revise the procedures for discovering and processing disaster relief assessments by: (1) regularly obtaining fire reports from all fire departments within the county; (2) maintaining better control of disaster relief claims; and (3) initiating a consistent procedure for granting relief when no application is returned. (Page 10)*

RESPONSE: We concur. Discussions have already taken place with the fire districts to determine the best way to implement this recommendation. We note, however, that the number of assessments affected is low. We would also note that when the new computer system is fully functional, tracking and reporting will be much easier and more efficient.

RECOMMENDATION 2: *Add the cash equivalent value of improvement bonds to the nominal sale price of properties. (Page 15)*

RESPONSE: Assessors are to enroll at the time of sale or new construction the full cash value of the property as defined in Revenue and Taxation Code Section 110. While Property Tax Rule 4(b) directs assessors to value the unencumbered fee interest and to make cash equivalencies, subdivision (d) of the same rule states the assessor shall "Make such allowances as he deems appropriate for differences between a comparable property and the subject property on the valuation date...". While cash equivalencies should be and are examined by the appraisal staff, ultimately the proper value is to be determined by consideration of all market factors, not by mechanically applying any formula for adjusting upward or downward what are, after all, minor amounts.

RECOMMENDATION 3: *Obtain copies of leases involving commercial properties. (Page 16)*

RESPONSE: We concur, and have been gathering such data since early in the current Assessor's term.

RECOMMENDATION 4: *Revise the procedures for assessing new construction by: (1) including the value of water wells and septic systems*

*in the assessments of single family residential properties;
(2) applying appropriate depreciation to new additions;
and (3) deducting the current assessed value of all
improvements removed as a result of new construction.
Page 18)*

RESPONSE:

(1): Our review of standard sewer/water hookups where available versus septic/well costs indicate that very little value difference exists, and that therefore using standard costs accurately reflect local market conditions. (2): Our appraisers are aware of the necessity of properly enrolling values for additions. Mechanically taking depreciation does not necessarily result in a proper assessment. For example, a residential addition may exist on a newly remodeled home, where the remodeling does not reach the level required for reassessment. In this instance, no allowance for depreciation on the addition would be proper. (3): We concur.

RECOMMENDATION 5:

Revise CLCA assessments by: (1) deducting a charge for return on and of the investment in irrigation systems from the total property income; and (2) deducting a charge for capital replacement of irrigation wells that contribute to the income being capitalized. (Page 21)

RESPONSE:

We concur, while noting that irrigation is found on a minority of our CLCA properties.

RECOMMENDATION 6:

Revise the assessment of CLCA and TPZ parcels by using a nine year term to prepare the first assessment after a notice of nonrenewal has been filed. (Page 23)

RESPONSE

We concur.

RECOMMENDATION 7:

Assess land subject to the provisions of Article XIII section 11 of the California Constitution at the lowest of current market value, Article XIII A factored base year value, or section 11 value. (Page 23)

RESPONSE:

We concur.

RECOMMENDATION 8:

Do not classify life estates as possessory interests. (Page 24)

RESPONSE:

We concur.

RECOMMENDATION 9: *Assess private water company property at the lower of market value or factored base year value. (Page 25)*

RESPONSE: We concur.

RECOMMENDATION 10: *Notify the county auditor of possible supplemental assessments caused by new construction. (Page 26)*

RESPONSE: The new property tax system will accommodate this recommendation automatically.

RECOMMENDATION 11: *Revise business property valuation procedures by: (1) assessing property based on reported costs on annual business property statements; (2) using cost indices and percent good factors that are contemporaneous with the current lien date; and (3) discontinuing the practice of limiting the percent good in depreciation tables to an arbitrary minimum level. (Page 29)*

RESPONSE: (1) Humboldt County does assess property based on costs reported on the Business Property Statement. The only exceptions are: (a) When businesses are sold the costs allocated to fixtures, machinery, and equipment are generally over or under allocated. When true costs are known or available to the Assessor's staff, these costs are used. (b) Many times the costs reported are net of allowances or trade-ins. Again, if the Assessor's staff knows, or has the true cost data available, the known true costs are used. (2) With the implementation of the new data processing program our office will be using the current percent good factors found in AH 581. (3) Our staff uses minimum percent good factors that accurately reflect the true replacement value of business assets in place and in use. The only possible exceptions are the six and seven and one-half year life tables that will be revised.

RECOMMENDATION 12: *Assess computers by using the BOE's recommended factors. (Page 31)*

RESPONSE: The BOE's recommended factors for computer equipment were developed by individuals in metropolitan counties for firms that are using the most current and sophisticated equipment. Using these tables in Humboldt

County where much of the equipment is used for five to ten years and not updated nearly as frequently tends to under value the equipment, not over value it. A five (5) year unfactored life table is planned for use in the future.

RECOMMENDATION 13: *Comply with Property Tax Rule 461(d) when determining the proper appraisal unit for determination of taxable value; enroll the lower of the factored base year value or the current market value as the taxable value of each appraisal unit. (Page 32)*

RESPONSE: We concur.

RECOMMENDATION 14: *Assign a certified appraiser the responsibility of determining boat values. (Page 37)*

RESPONSE: We concur. A certified appraiser will assign values to the boats for 1998.

RECOMMENDATION 15: *Revise manufactured home assessments by: (1) classifying assessable manufactured homes on non-permanent foundations as personal property on the secured assessment roll; (2) enrolling the lower of the factored base year value or the current market value as the taxable value of all assessable manufactured homes; and (3) not applying the Article XIII A inflation factor to a prior year's market value estimate. (Page 39)*

RESPONSE: We concur. The conversion process to the new property system will entail identification by foundation type of all manufactured homes. Those on permanent foundations will be properly classified as improvements; those not on permanent foundations will be classified as manufactured homes, personal property.